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RUEHBR/AMEMBASSY BRASILIA 5821
RUEHBU/AMEMBASSY BUENOS AIRES 1516
RUEHLP/AMEMBASSY LA PAZ 2406
RUEHPE/AMEMBASSY LIMA 0660
RUEHMN/AMEMBASSY MONTEVIDEO 0881
RUEHQT/AMEMBASSY QUITO 2492
RUEHSG/AMEMBASSY SANTIAGO 3824
RUEHAO/AMCONSUL CURACAO 1062
RUEHGL/AMCONSUL GUAYAQUIL 0711
RUEATRS/DEPT OF TREASURY
RUCPDOC/DEPT OF COMMERCE
RUMIAAA/HQ USSOUTHCOM MIAMI FL
RHEHNSC/NSC WASHDC

UNCLAS SECTION 01 OF 03 CARACAS 003411

SIPDIS

SENSITIVE
SIPDIS

TREASURY FOR KLINGENSMITH AND NGRANT
COMMERCE FOR 4431/MAC/WH/MCAMERON
NSC FOR DTOMLINSON
HQ SOUTHCOM ALSO FOR POLAD

E.O. 12958: N/A
TAGS: ECON EFIN VE
SUBJECT: SAVING FOR A RAINY DAY? BRV ACCUMULATES CASH RESERVES

REF: A. CARACAS 01291

¶B. CARACAS 02718
¶C. CARACAS 2622
¶D. CARACAS 3316
¶E. CARACAS 3374

¶1. (SBU) SUMMARY: Embassy estimates are that the BRV currently has between USD 40 and 50 billion in available funds, apart from the USD 35 billion in foreign exchange reserves, distributed between the Central Bank (BCV) and private and public sector banks. These funds represent "excess" oil revenues, pilfered foreign reserves, and unspent government funds and could cover government expenditures for 9-11 months. The fact that this huge, opaque reserve exists is demonstrative of Chavez's propensity for parallel networks, desire for a security blanket of money following the 2002 coup and 2002-2003 strikes, and is representative of the inherent corruption and dysfunctionality of the BRV bureaucracy.

SEVEN YEARS OF PLENTY

¶2. (SBU) The price for the Venezuelan oil basket has risen from USD 11 when Chavez came into office in 1999 to USD 57.19 on November 10, and BRV spending has increased over 100 percent (in dollar terms) and over 700 percent (in Bolivars) during his tenure. The BRV is also hoarding money. While these transactions are intentionally opaque, current Embassy estimates are that the BRV had around USD 41 billion as of the end of August in available funds in addition to the BCV foreign exchange reserves. (Note: Our estimate is lower than many other local economic consultancies, which estimate around USD 45-48 billion. Our estimate represents an 18% increase from April 2006 (see reftel A). End Note.) This amount is divided between treasury funds held in the BCV (USD

5.7 billion), BRV deposits in private sector banks (USD 9.1 billion), The Bank for Social and Economic Development (BANDES) (USD 10.2 billion), the Fund for National Development (FONDEN) (USD 14 billion, held by the Treasury Bank) and the Fund for Social and Economic Development (FONDESPA) (USD 2 billion). (Note: These numbers are gleaned from BCV reports and public comments by BRV officials. There is some doubt as to the accuracy of BRV financial accounting and many reports are significantly late. End Note.) (Comment: In addition to the rainy day funds and official reserves, PDVSA has tens of millions of dollars in escrow accounts tied to the Faja strategic associations. PDVSA can only draw on the accounts by presenting audited financial statements. It is very possible that PDVSA has additional funds held in off-shore accounts, but we have no way of verifying their existence. End Comment.)

¶3. (SBU) These funds have varying degrees of availability. BRV funds held in treasury accounts at the BCV represent government revenues not yet expended and technically cannot be spent without National Assembly (AN) approval. The AN has authorized almost USD 14 billion in additional credits (9 percent of GDP) in 2006 and this money remains in treasury accounts until requested by the relevant ministry or agency. (Comment: It is unlikely that the BRV will be able to spend all of this money due to bureaucratic inefficiency and capacity problems (see reftel D). We also note that PDVSA has had problems in the past executing on its investment budget. End Comment.) If the money is not spent in 2006, it will have to be re-authorized as an additional credit to the 2007 budget. The BCV is holding around USD 5.7 billion in treasury accounts.

¶4. (SBU) Another result of BRV inability to absorb and spend all of its authorizations has been for ministries and government institutions to store their money in private sector banks. Fifteen of the 50 active Venezuelan financial institutions count on 30 percent or more of their deposits from the BRV and thus are more or less reliant on BRV deposits for profitability, if not solvency. This dependency has led to widespread corruption, wherein banks pay off government officials to obtain deposits and to ensure that they stay in place. (Comment: A large-scale withdrawal of BRV funds could precipitate a banking crisis as the banks dependent on government deposits begin to fail, which could snowball as the Venezuelan banking system has many inter-bank ties and off-the-books relationships (see reftel C). Such a dependence on government deposits also gives BRV officials leverage over a large portion of the banking sector. End Comment.) Our current estimates are that there are USD 9-10 billion in private sector banks (representing about 1/5 of the assets of the Venezuelan banking sector). This does not include trust funds and other off balance sheet financial holdings by the banking sector.

¶5. (U) BANDES is a public sector bank run by the Vice Minister of Finance Behrens. Originally founded as the Venezuelan Investment Fund in 1974, it was revived by Chavez in 2001 and renamed. BANDES received cash infusions from PDVSA after its re-constitution, but has since been nominally independent. Its deposits, while not intended for budgetary spending, could easily cover for potential shortfalls by paying for projects that the government found itself incapable of funding. At the end of August, 2006 BANDES had USD 10.2 billion in assets and USD 736 million in outstanding loans.

¶6. (U) FONDEN and FONDESPA essentially function as a parallel budget subject to Chavez's whims, and already cover budgetary shortfalls (for example by funding portions of the missions) (see reftel A). FONDEN received USD 4.2 billion from BCV reserves over the past year and is receiving between USD 120 and 200 million weekly from PDVSA. It currently has about USD 14 billion in assets. (Note: Chavez has returned

to the "excess" foreign reserves theme and expectations are that, if re-elected, he will demand another transfer of USD 5-6 billion from the BCV to FONDEN early in 2007. End Note.) FONDEN is expected to spend USD 6-8 billion in 2006 and FONDEN's assets are held in the Treasury Bank in trust funds.

¶7. (U) In addition to these parallel mechanisms, PDVSA spent USD 5.384 billion in 2005 on "social expenses" and spending in 2006 should be even higher than in 2005 due to the higher average oil price USD 46.03 (for the Venezuelan basket in 2005) instead of USD 57.19 (the Venezuelan basket so far in 2006) and increased PDVSA participation in social activities. (Comment: PDVSA's duties seem to be branching out daily. In addition to being an oil company, it is now involved in agricultural projects (see reftel E), power generation, and the construction of infrastructure such as roads and schools. End Comment.)

SEVEN YEARS OF FAMINE?

¶8. (SBU) While experts differ as to whether the size of financial holdings is demonstrative merely of BRV incompetence or specific Chavez planning, these funds will give the BRV a solid cushion against possible future falling oil prices. Total BRV spending (including PDVSA social spending and FONDEN) could reach USD 60 billion in 2006 (39 percent of GDP). Spending has increased around 35 percent in

real terms in 2006 and has increased 100 percent in real terms since 1999. The consensus estimate for the Venezuelan oil basket next year is around USD 55, near this year's average, and oil production is not increasing. (Note: It is currently estimated at 2.4 to 2.6 million barrels/day. End Note.) (Comment: If government revenues remain steady (oil prices do not spike) and spending (including budget and parallel/off-budget) continues to increase, the BRV will begin to run significant deficits (in excess of 3 percent of GDP), starting as early as 2007. End Comment.)

¶9. (SBU) Comment: This cushion of USD 40-50 billion (USD 75-85 billion if international reserves at the BCV are included) provides a security blanket for Chavez and the BRV. If there are further economic disruptions or a sharp decrease in oil prices or production, Chavez will be able to maintain government services and spending and thus his base of support. A rough estimate is that even given a complete cessation of revenues (similar to the general strike of December 2002-January 2003), this money would allow the government to maintain current spending levels for nine months. Should the price of the Venezuelan oil basket fall below the USD 40 a barrel that most experts agree represents Venezuela's break even point, the excess funds could cover budgetary deficits for 2 years or more. End Comment.

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